Case Study: Barbados and The International Monetary Fund (IMF)

The Country:
Barbados is a Caribbean island country located in the Atlantic Ocean. It was uninhabited when the British settled it in 1627. Slaves worked on colonial sugar plantations until slavery was abolished in 1834. Barbados became independent from Britain in 1966 and has been politically stable since then. Historically, the economy was dependent on the production of sugar cane, but during the 1990s tourism and light manufacturing became more important. Barbados also provides financial service for foreign businesses, which helps to bring in foreign currency.

The Problem:
The balance of payments (BOP) is a record of all the money coming into a country from abroad and all the money going out of a country to other countries during a specific time period, usually one year. For example, money come into Barbados when tourists send money there and when other countries import sugar from Barbados. Money goes out when people in Barbados buy foreign goods or make investments in other countries.

In the early 1990s the BOP deficit increased sharply; more money was going out of Barbados than coming in. This was due in part to a drop in tourism and a large increase in the government budget deficit. There weren’t enough foreign currency reserves to pay for the imports and other assets that people in Barbados wanted to buy from abroad. Inflation was on the rise; economic growth was stagnant, and unemployment was high. Barbados sought help from the IMF.

The IMF Supported Program:
Barbados requested financial assistance from the IMF, which is normally granted if the government implements an economic reform program designed to eliminate the underlying problems over time. The IMF supported program in Barbados focused on improving the economy through sound fiscal and monetary policies and on helping to make the country’s businesses more competitive in the world. The government tightened fiscal policy by drastically cutting its spending and improving the efficiency of the tax system. Wages of government workers were cut, and some government workers were laid off and encouraged to find work in the private sector. (This action was later ruled illegal, and the government had to restore wages when the economy improved.) The central bank used monetary policy to raise interest rates; this action discouraged excessive spending and reduced inflation. In the private sector a wage program which kept labor costs down was implemented. This meant that Barbados could keep down the prices of its exports and compete better with other countries. Its low prices also attracted tourists. All of these measures were designed to curtail inflation and improve long-term economic growth. This would attract more foreign currency to Barbados by increasing exports, tourism and foreign investment and would help to bring an end to the uns sustainable BOP deficit.

Although some of these measures sound harsh and might be unpopular, there are seldom many options for correcting a BOP deficit. One possible alternative would have been for Barbados to devalue its currency, resulting in lower prices for tourists in Barbados and those buying Barbados' exports. However, the government was committed to maintaining the value of the Barbados dollar, which was pegged to the U.S. dollar.

The Outcomes:
Barbados and the IMF achieved the desired goals in a relatively short period of time. The BOP deficit turned into a surplus, and reserves of international currency increased in 1993-94 due to increased tourism from Europe and a drop in government spending and the associated imports. A program was initiated to revive the sugar industry to increase exports. Although there were initial declines in GDP (with resulting increase in unemployment) due to the decrease in the size of the government sector, GDP growth picked up by 1994-95. Inflation fell to a very manageable rate of one percent. However, there is always a possibility that problems will arise again in the future because the Barbados economy relies heavily on tourism, which has its ups and downs.
Case Study: Estonia and The International Monetary Fund (IMF)

The Country:
Estonia is an Eastern European country bordered by the Baltic Sea, Latvia, and Russia. Estonia was forced in the Soviet Union in 1940 and remained under communist control until 1991 when the Soviet Union broke up. Along with other former Soviet Republics, Estonia is a transition economy; it is in the process of changing from a planned economic system to a market economic system. Estonia is considered one of the most economically free and successful former Soviet Republics, and was admitted to the European Union in 2004.

The Problem:
The early years of transition were difficult in Estonia and the other former Soviet Republics. The economy experienced 900 percent inflation in 1992, a year after the economy switched to a free market system. This means that on average what cost 100 Estonian kroons in 1991 cost 1,000 kroons in 1992. Production fell 20 percent, resulting in decline in income. However, unemployment was not as high as expected due to emigration to Western countries. Estonia's problems were caused in part by the shocks associated with the break in the trade and financial links that had existed within the Soviet Union and the lag in establishing a functioning market economy. Although Estonians desperately wanted to have a free market economy, they lacked the skills, experience and institutions necessary for such an economy to function.

The IMF Supported Program:
It has been a challenge for the IMF to help Estonia and other former communist countries reorient their economies toward market systems and become integrated into the global economy. The IMF provides advice and assistance to help liberalize and privatize the economies: to end price controls and replace government ownership with private ownership. The IMF also provides advice and assistance to help stabilize the economies by controlling inflation and unemployment and promoting economic growth. The IMF assists in restructuring the economies by guiding the process of establishing institutions such as banks that are necessary if the new markets are to function.

The first IMF supported program for Estonia was approved in 1992, and was aimed at macroeconomic stabilization and the establishment of institutions to ease the transition to a market economic system. The IMF provided loans, policy advice, and technical assistance. Estonia established a currency board to control the money supply and stabilize its new currency through a fixed link with the Deutschemark, the German currency at the time. Estonia also avoided having a government budget deficit for a number of years, and introduced a policy to restrain wage increases. This policy kept down business costs and prices of goods for export, which encouraged other countries to import goods from Estonia.

The second phase of the IMF supported programs for Estonia took place from 1994 through 1998, and was directed toward increasing economic growth. After 1998 IMF assistance consisted only of advice and technical assistance; Estonia did not need to draw on the loan funds available. From 199 through 2003, the goals were to continue to help the Estonian economy develop and qualify for admission into the European Union.

The Outcomes:
Estonia is viewed as having successfully made the transition from a planned to a market economy, while bringing inflation under control and promoting economic growth. Estonia’s rate of inflation fell to 35 percent in 1995 and as of 2004 was less than 3 percent. The success in curtailing inflation is attributed to the successful operations of the currency board. Compared to other transition economies, real GDP recovered from its initial declines quickly, and as of 2004 was increasing at rates averaging 6 percent annually. Despite its successes, in 2004 the IMF was concerned about Estonia’s large current account deficit. This means that Estonia was spending more on imports than it earned by exporting goods.
Case Study: South Korea and The International Monetary Fund (IMF)

The Country:
The Republic of Korea, sometimes called South Korea, is an East Asian country on the southern half of the Korean peninsula. It became a country after World War II when it was separated from communist-controlled North Korea. South Korea (along with Taiwan, Singapore, and Hong Kong) is one of the four “Asian Tigers,” countries that experienced very rapid economic growth from the 1970s through 1997. South Korea’s GDP per capita is 18 times higher than North Korea’s, and is equal to that of some European Union Countries.

The Problem:
An Asian financial crisis took place in 1997-98. It began in Thailand and rapidly spread to other countries, including Korea. This crisis exposed many underlying weaknesses in the Korea economy, which was dominated by large government-guided conglomerates called chaebols. In part because there was little public information on these conglomerates’ management and their real financial situation, investors lost confidence in Korea and with drew money from Korean stocks and other assets. The stock market plunged, and the country fell into a severe recession. The currency, the won, depreciated, and there was a significant risk of inflation. Many of the chaebols went bankrupt. Korea sought help from the IMF in November 1997 in the form of a three-year stand-by arrangement, a loan that the country could borrow from as needed.

The IMF Supported Program:
On December 4, 1997, the IMF approved Korea’s request for a loan to support economic reforms. The IMF provided assistance under the Emergency Financing Mechanism, which allowed Korea to receive the money very quickly because of the crisis. The reforms were designed to help Korea recover from the Asian financial crisis and to correct some of the underlying problems in its economy. Overall objectives of the IMF supported program included restoring the confidence of investors in the economy, restoring GDP growth, containing inflation, and building up reserves of international currencies. Responding to advice from the IMF, the government pledged to conduct monetary policy to aim for an inflation of 5 percent and to stabilize the value of the won, to keep government spending under control and to encourage freer trade by eliminating subsidies to domestic businesses that protected them from foreign competition.

To reform the financial and business sectors of the economy, banks, other financial institutions, and businesses that were failing were closed rather than supported by the government. Financial supervision and accounting practices were raised to international standards. Financial statements were open to audits by internationally recognized firms. Foreign investment was allowed in businesses where it had been prohibited.

The Outcomes:
Korea implemented strong reforms and macroeconomic policies recommended by the IMF. As a result, its economic growth picked up quickly, and inflation was kept in check. Korea did not borrow all the funds available under the loan agreement and actually repaid substantial amounts earlier than scheduled.

The Asian financial crisis presented a new situation for the IMF. Many people, including those inside the IMF, believe that in the future more should be done to deal with underlying economic weaknesses with the goal of preventing crises. Whether this is always possible is a difficult question.
Case Study: Turkey and The International Monetary Fund (IMF)

The Country:
Turkey is located in both Europe and Asia at the northeast end of the Mediterranean Sea. Modern Turkey was founded in 1923 from parts of the former Ottoman Empire. There were several military coups in Turkey during the twentieth century, but civilian governments were always able to regain political power. Turkey’s economy is a mix of modern industry and traditional agriculture that accounts for 40 percent of Turkish employment. As of 2005, Turkey was striving to undertake the legal and economic reforms necessary to qualify for membership in the European Union.

The Problem:
High and volatile inflation has been Turkey’s main economic problem. Since about 1980 it has averaged between 40 and 100 percent per year with peaks of over 100 percent. (An annual inflation rate of 100 percent mean that the average level of prices doubles every year.) This high rate of inflation resulted from loose fiscal policy, including overly generous social security benefits and large agricultural subsidies. These payments led to very large government budget deficits. When a government spends more than it takes in from tax revenues, it has budget deficits, which need to be financed. In Turkey this has been done through loans from foreigners and by the central bank printing money, which causes inflation. In the 1990s it became evident to economists, private businesses, and the IMF that a reduction in inflation would greatly benefit the Turkish economy. Lower inflation would lead to increased confidence in the economy, more foreign investment, and higher and more stable economic growth.

The IMF Supported Program:
Since 1980 Turkey has had a series of IMF supported programs designed to control inflation and strengthen the economy. An ambitious set of reforms with IMF loans and assistance had good initial results. But by 1989 the problems of increasing inflation and an increasing government deficit arose again. This failure was due in part to the Turkish government’s inability to control spending as prescribed in the IMF plan. Between 1994 and 2004, Turkey and the IMF tried a number of times to agree on a program to control inflation. These programs were not successful initially because they were not implemented fully, but since 2001 results have been more positive.

These more successful reforms have included attempts to reduce government spending by reducing the size of the government workforce, privatizing businesses formerly owned by the government, restraining government workers pay increases, and reforming the social security system. Efforts have also been underway to reform the tax system to close tax loopholes and improve the efficiency of tax collections. In these ways, the government has lowered its deficit by decreasing spending and increasing tax revenues. In addition, the central bank has been granted independence and given price stability as its primary objective and has been freed from the obligation of printing money to finance the budget deficit. Finally, the IMF granted substantial financial assistance to support Turkey’s balance of payments.

The IMF supported programs to improve fiscal policy and lower inflation in Turkey have been criticized because they have taken a long time to take effect. Outside events such as political turmoil in 1997 have hindered the efforts, and at times the government has not been fully supportive of the proposed reforms. However, since 2001 the reforms have been fully implemented and appear to be working.

The Outcomes:
Turkey’s GDP growth averaged a healthy 6-7 percent in 2002-04, and inflation decreased from 70 percent in 2000 to less than 10 percent in 2004. This success is attribute to Turkey’s following the strong macroeconomic stabilization policies supported by the IMF. Concerns over fiscal policy remain, however, because Turkey’s government debt is still high.
Case Study: Uganda and The International Monetary Fund (IMF)

The Country:
Uganda is a landlocked country in East Africa with a troubled history. It was a British colony until 1962. From 1970 to 1985, its leaders were known for human rights abuses, causing the death of over a half million of its people. However, since coming to power in 1986, President Yoweri Museveni has introduced reforms, improved the country’s human rights record, and introduced IMF supported programs that greatly improved the economy. Despite this progress, Uganda faces many challenges.

The Problem:
In 1996 and 1997 Uganda sought the help of the IMF to reduce the large debts that it owed to foreign countries and banks. When a country has a foreign debt, it had to pay interest on the debt, as well as part of the principal every year. This meant that Uganda could not use this money to pay for clean water, medicine, education, and road maintenance. Uganda’s large debt also meant that foreign private investors were unlikely to want to invest in the country because of the risk that they would not get their money back. It was important for Uganda to reduce the amount of its foreign debt, so it could use the money to fight poverty. Uganda was one of the poorest countries in the world, with an estimated 44 percent of its population living in poverty. The problem of poverty in Uganda is related to problems in education and health. Many children drop out of school due to a lack of money. There are widespread health problems due to limited access to clean water, doctors, medicine, and transportation.

The IMF Supported Program:
In 1997 Uganda was one of the first countries to qualify for IMF assistance under the Heavily Indebted Poor Country (HIPC) program. Under this program foreign countries and banks agree to cut the amount a country owes them by a large amount provided the country effectively implements an antipoverty program. Uganda qualified for the IMF HIPC program because it demonstrated that it followed good economic policies during the three-year period prior to 1997. One of the main goals of this program is to give countries debt relief (meaning they do not need to pay back some prior loans) so they have more money to spend on reducing poverty and promoting economic growth.

As a result of the HIPC program, Uganda committed to support economic growth and to make sure that poor people directly benefited from the improved economy. Economic growth can help reduce poverty because it results in more jobs, higher incomes, and more goods and services for the population. Uganda’s poverty-reduction programs included privatizing businesses that had been run by the government, improving communication and transportation networks, helping export industries (coffee is Uganda’s chief export) and providing universal access to health care and education. The Ugandan government also created a Poverty Action Fund as part of its budget to monitor antipoverty programs carried out under the HIPC program. This makes it easy to ensure that Uganda used the money it saved from the debt reduction on health, education, and other poverty-reduction programs. Because Uganda met all the commitments under the HIPC program, in 2000 it was one of the first countries to receive substantial reduction in its foreign debt under an enhanced HIPC debt-relief program.

The Outcomes:
The outcomes of Uganda’s efforts to reduce poverty within the IMF supported program and with the support of foreign countries and banks are encouraging, and Uganda is viewed as a successful model for the IMF HIPC program. As of 2004, Uganda was experiencing strong economic growth, low inflation and increases in exports. Statistics show that poverty had been reduced over the past 10 years or so. Furthermore, support from the IMF, including the HIPC, helped Uganda to gain credibility among other international donors, that are now providing very significant aid to Uganda. Despite these gains, Uganda is still a poor country facing problems with HIV/AIDS, rebel forces and government corruption. Much has been accomplished, and much remains to be done.